Overview on Mergers & Acquisitions

Western India Regional Council of
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M&A – Introduction

- Liberalization of economy and reform programmes have resulted in a 'churn' in the industrial and services sector

- Companies are resorting to acquisitions as a means to consolidate and grow rapidly

- Globalization has given importance to size for competing effectively with the multinationals and exploring the world markets

- As a result, there is a manifold increase in the level of M&A activity in last two decades

M&A – Global Scenario

- The era of volatility has made it inevitable for a business to grow through in-organic means

- After a consecutive year-on-year (“YoY”) increase in M&A globally for 3 years, it declined YOY in 2016.

- Interestingly in India, M&A saw a YoY increase in 2016 with most deals focussed over the IT and Internet sector. However, in terms of value, increase was the highest in finance and insurance sector.

What is M&A?

Mergers & Acquisitions

- In common parlance, **merger** means combination of two or more commercial organizations into one. It is fusion of two or more existing companies

- An **acquisition**, also known as a takeover, is the buying of a business or a company (the 'target') by another. It can be done mainly through 2 modes:
  - Business Purchase
  - Share Purchase

Few Recent Deals

Type	Acquiror	Target	Sector	Value (USD Mn)	Deal Type	Stake
Domestic	Ultratech Cements Limited	Jaiprakash Associates Limited	Manufacturing	2,373.13	Acquisition	100%
	Tata Power Renewable Energy Limited	Welspun Renewable Energy Private Limited	Energy and natural resources	1,380.45	Acquisition	100%
Inbound	The Yokohama Rubber Co. Limited	Alliance Tire Group	Automotive	1,200.00	Majority Stake	90%
	Singapore Technologies Telemedia	Tata Communications Data Centre Private Limited	IT and ITeS	616.00	Majority Stake	74%
Outbound	Indian Oil Corp. Limited, Oil India Limited and a unit of Bharat Petroleum Corp. Limited	Tass-Yuryakh oilfield	Energy and natural resources	1,286.76	Strategic Stake	30%
	Wipro Limited	Healthplan Services	IT and ITeS	460.00	Acquisition	100%

Drivers of M&A

Drivers of M&A

The major drivers of M&A mainly from the perspective of the seller are as follows:

- Consolidation
  - E.g. The entry of Reliance Jio has led to consolidation in the telecom sector. As a result Idea and Vodafone consolidate their operations
- Sale of non-core assets, mainly to reduce debt
  - E.g. Jaypee group has sold its cement units and power units mainly to reduce debt
  - Reliance Communications sells its Tower Business to Brookefield mainly to reduce debt
- Regulatory Considerations

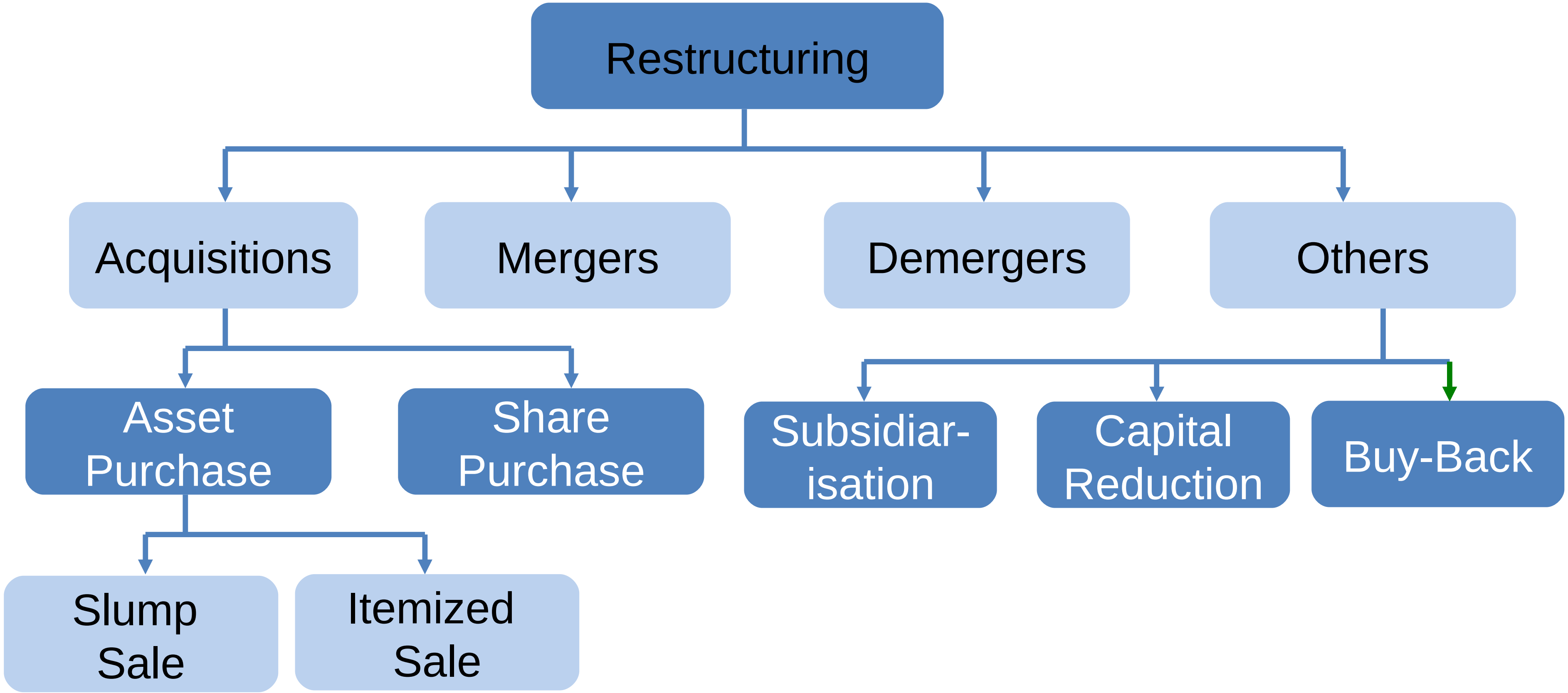
Corporate Restructuring

Corporate Restructuring

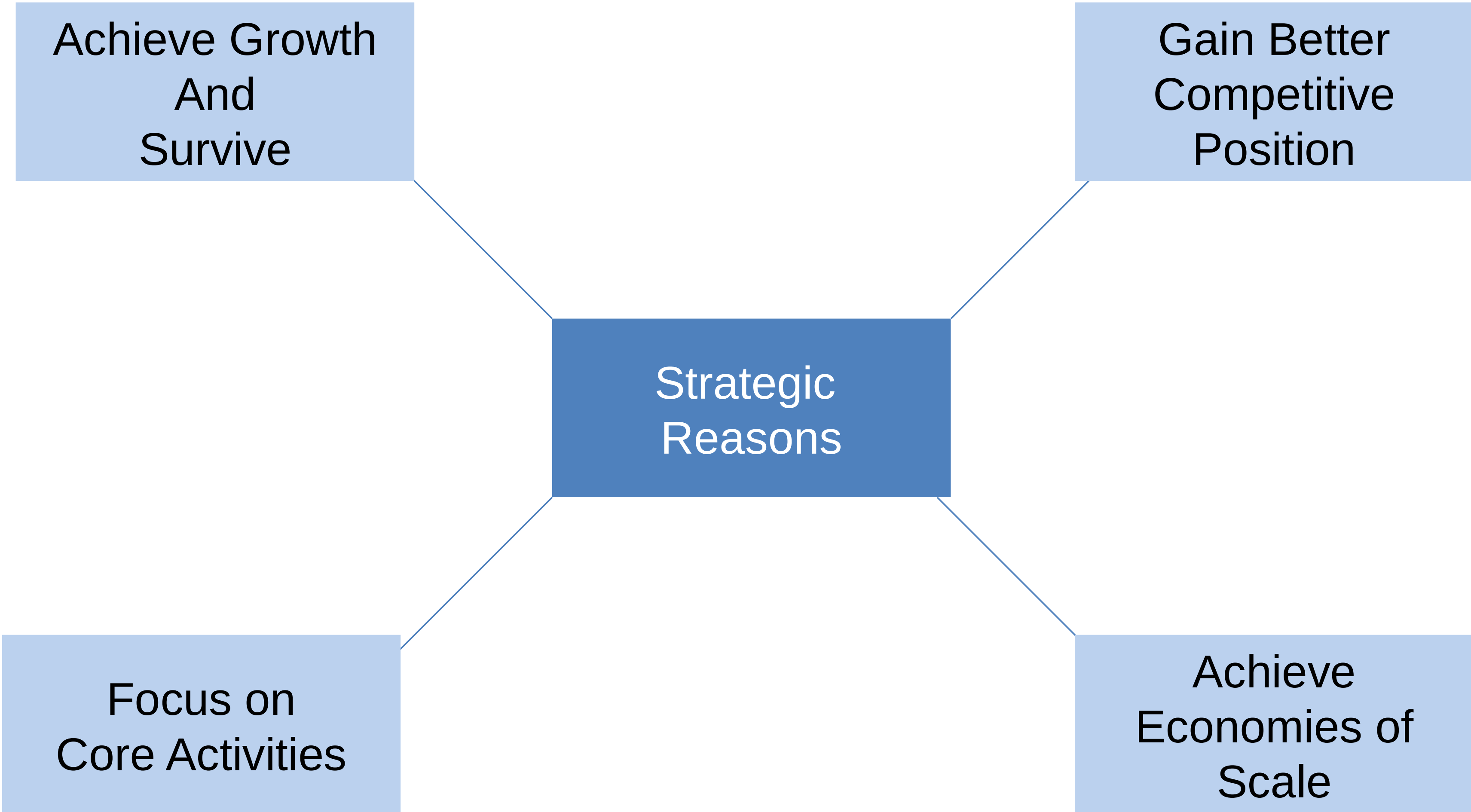
- One of the dictionary meaning of “Restructuring” is “Rearrangement”
- Rearrangement of corporate structure
- Process by which a business organizations alters its present structure in order to create a new structure in place of existing structure
- Corporate Restructuring may involve change in asset structure, liability structure or both

Types - Based on purpose

Modes of Restructuring



Motives of Restructuring



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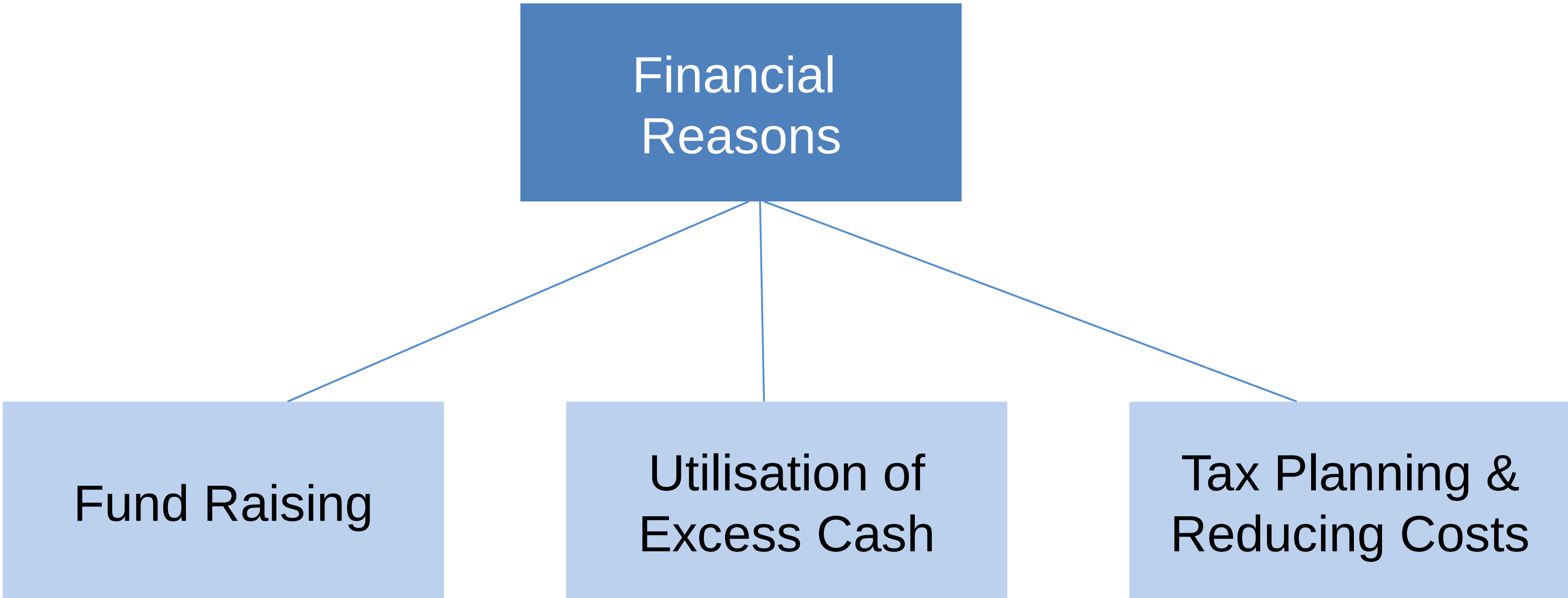


Motives of Restructuring

Other Reasons

- Bail Out 'Takeovers'
- Diversification – Entering into a new segment
- Family Separation
- Fall out of Global event

Merger

- In common parlance it means combination of two or more commercial organizations into one
- Merging company loses its separate identity
- It is fusion of two or more existing companies
- All assets and liabilities of one or more Companies are transferred to another Company
- Merger and Amalgamation terms are used interchangeably

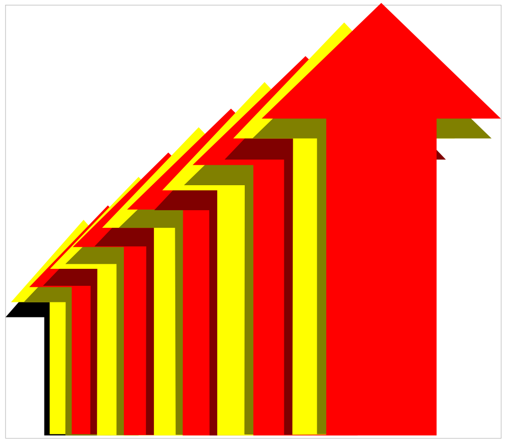
Types of mergers

Vertical Merger:

- Merger with suppliers or customers

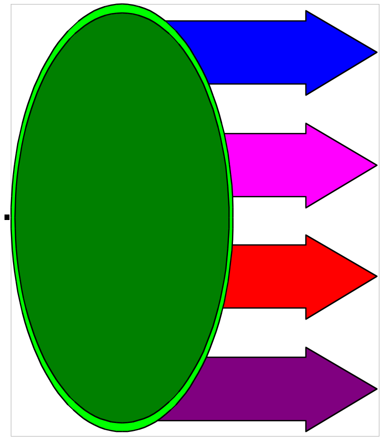
E.g. 1: Kochi Refineries Ltd Merges into Bharat Petroleum Corporation Limited

E.g. 2: Sterling Holiday Resorts (India) Limited merges into Thomas Cook (India) Limited



Types of mergers

Horizontal Merger:



- Between firms in the same kind of business usually as competitors.
- Generally has the effect of reducing competition

E.g.: Centurion Bank merger with HDFC Bank
Idea-Vodafone; RCom-Aircel

Types of mergers

Conglomerate Merger:

- Lines of business have nothing to do with one another

E.g.: Indo Gulf and
Birla Global Finance
merging into Indian Rayon.
New Co
rechristened Aditya Birla Nuvo

Points to be considered while contemplating M&A

- M&A - Terms
- M&A - Financing
- Break - even : Synergies
- Financial modelling
- Stress-testing and scenario analysis

Acquisition / Takeover

Acquisitions / Takeovers

Acquisitions / Takeovers:

- An acquisition, also known as a takeover, is the buying of a business or a company (the ‘target’) by another

Modes:

- **Business Purchase**: This type of transaction leaves the target company as an empty shell. It is further divided into:
  - Slump Sale
  - Itemized Sale

- **Share purchase**: The buyer buys the shares, and therefore control of the target company
  - *Example: Coromandel International acquires stake in Liberty*

Acquisitions / Takeovers

- **Slump Sale:** Section 2(42C) of the Income Tax Act, 1961 defines Slump Sale as the transfer of one or more undertakings as a result of the sale for a lump sum consideration without values being assigned to the individual assets and liabilities
  - *Example: Piramal Healthcare sold its domestic formulation business to US based multinational drug major Abbott in a deal worth ~ $ 3.8 Bn*

- **Itemized Sale:** Sale of assets & liabilities with values assigned separately for each item of assets & liabilities

- **Slump Sale vs. Itemized Sale:** In case of itemized sale, unlike slump sale, it is possible to pick and choose assets and liabilities. Also, the consideration is identifiable against each item

Types of Acquisitions

Acquisition - friendly or unfriendly

Friendly Takeovers:

Acquirer's contacts target's management & proposes a deal. Target agrees and cooperates

Unfriendly Takeovers:

Acquiring firm makes a tender offer to target's shareholders.

Difference Between Mergers & Acquisition

Merger

- Consideration discharged by issue of shares of Transferee co.
- Shareholders of Transferor co. become shareholders of Transferee co.
- Usually by negotiations

Acquisition

- Consideration may be by cash or shares
- Acquirer co. gains controlling interest in the Target co.
- May be friendly or hostile

Other modes of restructuring

Demerger

- Demerger contemplates hiving off a division/unit/business of a company into a new/existing company

- Demerger involves a vertical split of company, whereby business is transferred on a going concern basis to a new/existing company

- This division may either:
  - Form a new company and operate separately from the original one, or
  - May get merged into another existing company

- Some common reasons behind a demerger are:
  - Unlocking shareholder value
  - Streamlining business segments
  - To make financial and managerial resources available for developing other more profitable

Slump Sale

- The term ‘slump sale’ connotes the sale of an entire business undertaking, comprising of various assets net of liabilities relating to the undertaking for a lump sum or ‘slump’ consideration. (Section 2(42C) of IT Act)

- The consideration may be discharged by issuing shares and/or cash to the Transferor co.

- A sale in order to constitute a slump sale must satisfy the following tests:
  - Business has been sold off as a whole and as a going concern
  - Sale for a lumpsum consideration
  - Materials available on record do not indicate item-wise value of the assets transferred

Subsidiarisation

- Subsidiarisation means transferring the business to a wholly owned subsidiary at book value or at fair value

- Companies resort to Subsidiarisation when the undertaking needs to be sold but there is no buyer ready to buy all the assets at a given point of time

- Under this option business gets transferred to a subsidiary and the parent company continues to hold 100% equity stake in the subsidiary. This option facilitates the process of disinvestment, as only the shares of subsidiary company will have to be handed over when the suitable buyer is found out.

- *Example: S. Kumars Nationwide Limited transferred its Reid & Taylor division to a subsidiary namely, Reid & Taylor (India) Limited*

Capital Reduction

- **Capital Reduction is the process of decreasing a company's shareholder equity through share cancellations and share repurchases so as to:**
  - increase shareholder value
  - produce a more efficient capital structure
- **Process u/s 66 of the Co.'s Act 2013 to be followed**
- **Situations in which a Co. may reduce its capital:**
  - Where the capital is unrepresented by assets
  - To return excess cash to its shareholders where there is no likelihood of the cash ever being required for the business

Buy Back

- **Buybacks is acquiring its own shares from the existing shareholders by the company to reduce its paid-up capital complying with provisions of sec.68 of the Co.'s Act, 2013**

- **Reasons for buy back include:**
  - putting unused cash to use
  - raising earnings per share
  - reduced equity base strengthens management control
  - increasing the value of shares (reducing supply)

- **Forms of buyback are as follows:**
  - From the existing security holders on a proportionate basis; or
  - From the open market; or
  - From odd lots.

Financing For Restructuring

Financing for Restructuring

There are various routes for financing a restructuring:

- Stock Financing Route
- Cash Financing Route
- Leveraged Buy-Outs (LBO)

Implications of M&A

Implications

The following factors should be kept in mind during restructuring:

- **Regulatory Considerations**
  - Companies Act, 2013 *(sec.230 to 240)*
  - SEBI & Other Capital Market Regulations
  - FEMA Guidelines
- **Accounting** *(IND-AS 103: Business Combinations)*
- **Income Tax**
- **Stamp Duty**
- **Sales Tax**
- **Excise Duty**

What may go wrong?

Pitfalls of M & A

Reasons why M & A may fail:

- Cultural Clash
- Wrong/Improper estimates
- Contractual limitations
- Synergies not well understood
- Loss of Key talent
- Inability to sustain financial performance
- In case of M&A for consolidation, the acquired business may compete with our existing business. However exceptions like Coca Cola and Thumps Up also exist.
- If acquired business is relatively small, it may not get due

Conclusion

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- While for some it may be beneficial to expand ownership boundaries through mergers and acquisitions. For others, separating the public ownership of a subsidiary or business segment offers more advantages.

- Merger may not be always successful but it surely delivers enhanced market power.

- Before executing any deal, a complete analysis of the associated costs and benefits should be carried out.


Thank you!